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PAGE 01 BELGRA 02494 01 OF 02 201532Z

47

ACTION EUR-12

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SUBJECT: GOVERNOR OF NATIONAL BANK OF YUGOSLAVIA AND ASSISTANT
SECRETARY OF FINANCE HOLD DISCUSSIONS WITH US BANKERS

SUMMARY: FOLLOWING ARE HIGHLIGHTS OF COMMENTS BY GOVERNOR
OF NATIONAL BANK COLANOVIC AND ASSISTANT SECRETARY OF FINANCE
STOJILKOVIC DURING BRIEFINGS AND QUESTIONS AND ANSWER SESSIONS
WITH US BANKERS VISITING YUGOSLAVIA IN CONNECTION WITH JOINT
CHAMBER OF COMMERCE MEETING (SEPTTEL). BOTH EMPHASIZED
YUGOSLAV POLICY OF EXPANDING ALL FORMS OF ECONOMIC COOPERATION
WITH US. IN DISCUSSING YUGOSLAV ECONOMIC TRENDS COLANOVIC SAID
CONTROL OF INVESTMENT SPENDING IS THE MAJOR POLICY GOAL OF
YUGOSLAV GOVERNMENT IN 1975. EMPLOYMENT AND PRODUCTION ARE
INCREASING PERHAPS TOO RAPIDLY, AGGRAVATING INFLATION AND BALANCE
OF TRADE DEFICIT. WEAK EXPORT PERFORMANCE TO WESTERN
EUROPE IS MOST TROUBLESOME ASPECT OF YUGOSLAV FOREIGN TRADE
IN 1975 AND COLANOVIC DOES NOT EXPECT MARKET CONDITIONS IN EEC
TO IMPROVE SUFFICIENTLY TO SPUR YUGOSLAV EXPORTS BEFORE SECOND
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PAGE 02 BELGRA 02494 01 OF 02 201532Z

HALF 1976. CURRENT ACCOUNT DEFICIT IN 1975 ESTIMATED AT

LEAST \$900 MILLION BUT NATIONAL BANK BELIEVES DEFICIT WILL BE FINANCED WITHOUT DRAWING DOWN YUGOSLAV RESERVES OF \$1.3 BILLION. ECONOMIC COOPERATION WITH ARAB OIL PRODUCERS AND CONSTRUCTION CONTRACTS WITH LDC'S ARE IMPORTANT PILLARS OF ECONOMIC POLICY OF 1975 AND BEYOND. WORKERS' REMITTANCES FORECAST TO RISE AGAIN IN 1975 WITH EARNINGS FROM THIS SOURCE EXPECTED TO PEAK 1978-79. NATIONAL BANK ESTIMATES NET RETURN FLOW OF ONLY ABOUT 20,000 YUGOSLAV WORKERS FROM WESTERN EUROPE THIS YEAR. COLANOVIC SAID NEW JOINT VENTURE LEGISLATION, LIBERALIZING PROFIT REMITTANCE WILL BE ENACTED IN 1975. NATIONAL BANK PLANS CONCLUDE AGREEMENTS WITH SOME EUROPEAN BANKS TO ALLOW DINAR CONVERTIBILITY WITHIN AGREED QUOTAS.

STOJILKOVIC EMPHASIZED NECESSITY FIND PRACTICAL WAYS IMPROVE ECONOMIC RELATIONS BETWEEN US-YUGOSLAVIA, ESPECIALLY COOPERATION IN THIRD COUNTRIES. HE SUGGESTED GROUP US SPECIALISTS SHOULD VISIT YUGOSLAVIA TO MEET WITH YUGOSLAV FIRMS WHICH HAVE EXPERIENCE IN LDCS. END SUMMARY.

1. COLANOVIC CHARACTERIZED STAGNANT YUGOSLAV EXPORTS TO EEC AS MOST TROUBLESOME ASPECT OF YUGOSLAV FOREIGN TRADE PERFORMANCE IN 1975. (VOLUME YUGOSLAV EXPORTS TO EEC DECLINED IN FIRST FOUR MONTHS 1975.) EXPORTS TO SOCIALIST COUNTRIES AND LDCS ARE GROWING, BUT COLANOVIC SAID WEST EUROPEAN COUNTRIES SIMPLY ARE NOT BUYING YUGOSLAV GOODS. HE DOES NOT FORESEE REVIVAL OF WESTERN EUROPEAN ECONOMIES SUFFICIENT TO SPUR YUGOSLAV EXPORTS BEFORE SECOND HALF 1976. IN THIS SITUATION HE CHARACTERIZED POSSIBLE DEVALUATION AS A "NONSENSICAL" POLICY WHICH WOULD NOT ASSIST EXPORTS.

2. IMPORTS HAVE SLOWED MARKEDLY IN FIRST QUARTER 1975 BUT COLANOVIC BELIEVES IMPORT GROWTH MAY RISE LATER IN YEAR. A POSITIVE NOTE IS THAT YUGOSLAVIA WILL NOT IMPORT GRAIN IN 1975 DUE TO EXCELLENT HARVESTS IN 1974 AND HIGH RESERVE LEVELS.

3. DISCUSSING INVISIBLE EARNINGS COLANOVIC SAID WORKERS REMITTANCES SHOULD INCREASE MODERATELY IN 1975 DESPITE SMALL NET RETURN OF YUGOSLAV WORKERS FROM WESTERN EUROPE. INCREASES ARE DUE TO HIGHER PER CAPITA EARNINGS AND SAVINGS AND SUCCESSFUL YUGOSLAV BANKING PROGRAMS TO ATTRACT YUGOSLAV WORKER SAVINGS IN LIMITED OFFICIAL USE

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PAGE 03 BELGRA 02494 01 OF 02 201532Z

GERMAN BANKS INTO YUGOSLAV BANKING SYSTEM. COLANOVIC BELIEVES WORKERS REMITTANCES WILL CONTINUE TO RISE UNTIL 1978 OR 1979 BY WHICH TIME EARNINGS FROM "BIG CONTRACTS" IN LDCS WILL BE IMPORTANT ADDITIONAL SOURCE OF INVISIBLE EARNINGS. RECEIPTS FROM TOURISM ARE EXPECTED TO REMAIN STABLE OR RISE SLIGHTLY IN 1975.

4. NATIONAL BANK CALCULATES AT LEAST \$900 MILLION DEFICIT ON CURRENT ACCOUNT IN 1975. COLANOVIC ACKNOWLEDGED SLACK EXPORTS

MAY INCREASE DEFICIT TO OVER \$1 BILLION BUT SAID YUGOSLAVIA WILL NOT HAVE TO DRAW DOWN RESERVES TO COVER TRADE DEFICIT. HE ENUMERATED SEVERAL CREDIT SOURCES THAT WILL HELP COVER DEFICIT: A) IMF OIL FACILITY - \$240 MILLION B) IBRD CREDITS OF ABOUT \$200 MILLION, C) DRAWDOWN ON 1974 WEST GERMAN 700 D.M. "REPARATIONS" CREDIT D) DIRECT CREDITS FROM OIL PRODUCERS, ESPECIALLY IRAQ, LIBYA AND KUWAIT, (COLANOVIC CONFIRMED IRAQ HAS SOLD YUGOSLAVIA LARGE AMOUNTS OF OIL FOR 1975 DELIVERY ON CREDIT), E) BOND ISSUE OF MODEST SIZE ON U.S. MARKET -- COLANOVIC ASKED US BANKERS' ASSISTANCE IN MAKING THIS A SUCCESS AND SAID MORE BOND ISSUES WOULD BE FORTHCOMING IF MARKET CONDITIONS WARRANT IT,--, F) SPECIAL DELIVERIES -- WHICH COLANOVIC DID NOT DEFINE BUT COULD MEAN RAW MATERIAL OR ADDITIONAL OIL IMPORTS WITH DEFERRED PAYMENTS.

5. COLANOVIC SAID YUGOSLAVIA DEBT SERVICE RATIO IS 15 PERCENT (TOTAL DEBT SERVICE AS PERCENTAGE OF TOTAL FOREIGN EXCHANGE EARNINGS)

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AND NATIONAL BANK PLANS HOLD DEBT SERVICE RATIO BELOW 15.5 PERCENT THRU 1980. FYI -- THIS STATEMENT ON DEBT SERVICE CONTRASTS SHARPLY WITH 20.9 PERCENT ESTIMATE GIVEN EMBASSY BY NATIONAL BANK SOURCE IN APRIL -- OBVIOUSLY DEFINITIONAL PROBLEMS ARE INVOLVED AND SPECIFIC INFORMATION IS NOT AVAILABLE. END FYI.

6. COLANOVIC SAID YUGOSLAVIA EXPECTS "IMPORTANT JOINT VENTURES IN AGRICULTURE WITH OIL PRODUCING COUNTRIES" IN 1975 AND 1976 WHICH WILL ASSIST BALANCE OF PAYMENTS. MOST FAVORABLE FACTOR IN ECONOMIC RELATIONS WITH LDCS IS CURRENT AND PROJECTED CONSTRUCTION CONTRACTS WHICH PROMISE SUBSTANTIAL LONG TERM BENEFITS.

7. YUGOSLAV FOREIGN EXCHANGE RESERVES ARE BETTER THAN NATIONAL BANK HAD HOPED EARLIER WITH CURRENT LEVEL FLUCTUATING BETWEEN 1.3 AND 1.5 BILLION DOLLARS. NATIONAL BANK BELIEVES TWO MONTH COVERAGE OF IMPORTS IS SUFFICIENT LEVEL OF RESERVES.
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PAGE 04 BELGRA 02494 01 OF 02 201532Z

8. NATIONAL BANK PLANS CONCLUDE AGREEMENT WITH SEVERAL EUROPEAN BANKS TO ALLOW LIMITED DINAR CONVERTIBILITY WITHIN AGREED UPON QUOTAS. COLANOVIC SAID NATIONAL BANK WOULD FOLLOW THIS EXPERIENCE CLOSELY AS GUIDE TO FUTURE ACTION ON DINAR CONVERTIBILITY.

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PAGE 01 BELGRA 02494 02 OF 02 201542Z

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LIMITED OFFICIAL USE SECTION 2 OF 2 BELGRADE 2494

9. COLANOVIC EMPHASIZED IMPORTANT ROLE US BANKS PLAY IN YUGOSLAV DEVELOPMENT PLANS AND HE ENCOURAGED US BANKERS TO ASK YUGOSLAV BANKS AND ENTERPRISES HOW THEIR LOAN APPLICATIONS FIT INTO YUGOSLAV INVESTMENT PLAN PRIORITIES (ENERGY, AGRICULTURE, STEEL, BASIC RAW MATERIALS, ETC).

10. ON DOMESTIC SIDE COLANOVIC SAID CONTROL OF INVESTMENT SPENDING IS NO. 1 PRIORITY OF YUGOSLAV ECONOMIC POLICY IN 1975. EXCESSIVE INVESTMENT SPENDING IS RESPONSIBLE FOR FUELING INFLATION AND STIMULATING EXCESSIVE IMPORTS. YUGOSLAVIA WILL ADOPT NEW LEGISLATION TO (A) RESTRICT NON-ECONOMIC INVESTMENT SPENDING AND (B) CHANNEL ECONOMIC SECTOR INVESTMENT INTO PRIORITY AREAS.

11. MONEY SUPPLY IN 1975 IS TO GROW AT LOWER RATE THAN INCREASE IN NOMINAL NATIONAL INCOME AND ACCORDING TO NATIONAL BANK CALCULATION THIS SHOULD HELP SLOW INVESTMENT SPENDING AND IN LONG RUN MODERATE INFLATION. COLANOVIC SAID IMPACT OF GROWTH OF MONEY SUPPLY ON PRICES HAS CONSIDERABLE TIME LAG (OVER ONE YEAR) IN YUGOSLAVIA. CONSEQUENTLY ECONOMY TO SOME EXTENT CONTINUES TO FEEL EFFECT OF LIMITED OFFICIAL USE

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PAGE 02 BELGRA 02494 02 OF 02 201542Z

HIGH MONETARY GROWTH IN 1972 AND 73 AND ONLY LATER THIS YEAR WILL 1974'S RELATIVELY SLOWER INCREASE IN MONEY SUPPLY HELP DAMPEN INFLATIONARY PRESSURES.

12. COLANOVIC NOTED THAT GROWTH OF PRODUCTION AND EMPLOYMENT MAY BE TOO HIGH FOR ECONOMY'S HEALTH SINCE THE BOOM EXACERBATES INFLATION AND ENCOURAGES IMPORTS (PRODUCTION INCREASED 9.5 PERCENT AND EMPLOYMENT 5.5 PERCENT IN FIRST FIVE MONTHS). HE SAID YUGOSLAV ECONOMIC POLICY WILL ATTEMPT TO SLOW GROWTH TO LEVELS ENUNCIATED IN RESOLUTION ON ECONOMIC AND SOCIAL POLICY OF 7.5 PERCENT IN PRODUCTION AND 3.5 PERCENT IN EMPLOYMENT. HOWEVER, HE ADDED THAT SOCIAL AND POLITICAL CONSEQUENCES OF COOLING OFF THE ECONOMY MAKES ACTION DIFFICULT.

13. COLANOVIC MAINTAINED 3.5 PERCENT INCREASE IN EMPLOYMENT WAS SUFFICIENT TO ABSORB NEW ENTRANTS TO LABOR FORCE FROM SCHOOLS, RURAL-URBAN MIGRATION, AND MODEST NUMBER OF WORKERS RETURNING FROM WESTERN EUROPE. NATIONAL BANK ESTIMATES THERE WILL BE NET RETURN FLOW OF 20,000 WORKERS IN 1975.

14. COLANOVIC DESCRIBED DRAMATIC POSITIVE CHANGES IN INVESTMENT, PRICE AND CREDIT POLICIES IN AGRICULTURAL SECTOR DURING PREVIOUS TWO YEARS NOTING THAT AGRICULTURAL SECTOR NOW OFFERS RETURNING WORKERS RENUMERATIVE EMPLOYMENT AND OPPORTUNITIES FOR INVESTMENT OF CAPITAL.

15. NEW JOINT VENTURE LEGISLATION IS TO BE ENACTED IN 1975 AND COLANOVIC STRONGLY SUGGESTED SIGNIFICANT LIBERALIZATION OF PROVISIONS GOVERNING PROFIT TRANSFER. HE SAID THAT IN 10 YEARS SINCE ORIGINAL JOINT VENTURE LEGISLATION PASSED THE DINAR HAS STRENGTHENED AND YUGOSLAVIA HAS GAINED EXPERIENCE IN FOREIGN ECONOMIC TRANSACTIONS AND CONSEQUENTLY "PHILOSOPHY OF JOINT VENTURES HAS COMPLETELY CHANGED". HE ADDED YUGOSLAV IDEAS HAVE GONE WELL BEYOND SIMPLY ALLOWING PROFIT TRANSFERS FROM IMPORT SUBSTITUTION INVESTMENT AND YUGOSLAVIA IS CONSIDERING ALLOWING REMISSION OF PROFITS EVEN FROM ORDINARY INVESTMENT FOR DOMESTIC MARKET.

16. ASSISTANT SECRETARY OF FINANCE STOJILKOVIC CONCENTRATED REMARKS ON NECESSITY TO FIND PRACTICAL WAYS TO A) IMPROVE OVERALL ECONOMIC RELATIONS BETWEEN US AND YUGOSLAVIA ESPECIALLY IN AREAS OF JOINT VENTURES AND TRADE AND B) GET LIMITED OFFICIAL USE

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PAGE 03 BELGRA 02494 02 OF 02 201542Z

YUGOSLAV-US COOPERATION ON CONSTRUCTION PROJECTS IN THIRD COUNTRY LDCS OFF THE GROUND.

17. STOJILKOVIC EMPHASIZED ROLE OF US BANKS IN FACILITATING CONTACTS BETWEEN US AND YUGOSLAV BUSINESSES AND IN GETTING ACCURATE INFORMATION ON YUGOSLAV ECONOMIC CONDITIONS AND OPPORTUNITIES TO US FIRMS.

18. AS TO COOPERATION IN LDCS STOJILKOVIC SUGGESTED US SEND MISSION FROM FIRMS SUCH AS BECHTEL TO YUGOSLAVIA TO MEET WITH YUGOSLAV FIRMS WITH EXPERIENCE IN LDCS. HE ASKED US

BANKERS AND OPIC TO STIMULATE US FIRMS TO PARTICIPATE IN SUCH A MISSION.

19. COMMENT: COLANOVIC'S REVIEW OF ECONOMIC TRENDS PRODUCED NO SURPRISES; IT WAS OF GREAT INTEREST AS UP TO DATE INDICATION OF OFFICIAL YUGOSLAV THINKING ON NUMBER OF IMPORTANT ECONOMIC PROBLEMS AND SOLUTIONS INCLUDING NECESSITY TO CONTROL INVESTMENT SPENDING AND IMPORTANCE OF INVISIBLE EARNINGS FROM CONSTRUCTION PROJECTS IN LDC'S. HE LEFT NO DOUBT YUGOSLAVIA EXPECTS ADDITIONAL CREDITS AND OTHER ECONOMIC BENEFITS FROM OIL PRODUCING COUNTRIES. HIS STATEMENT THAT YUGOSLAV RESERVES WOULD NOT HAVE TO BE DRAWN DOWN IN 1975 WAS PERSUASIVE, ESPECIALLY IN CONTEXT OF YUGOSLAV COOPERATION WITH OIL PRODUCERS. COLANOVIC'S VIRTUAL ADMISSION THAT TRADITIONAL POLICY TOOLS TO DEAL WITH STAGNATING EXPORTS TO WESTERN EUROPE ARE INEFFECTIVE SUGGEST YUGOSLAVIA MAY BE CONSIDERING ADDITIONAL DIPLOMATIC AS WELL AS ECONOMIC INITIATIVES TO HELP OFFSET THE SIZEABLE TRADE DEFICIT WITH EEC COUNTRIES. CONVERSATIONS WITH VISITING US BANKERS, RECENT YUGOSLAV-GERMAN NEGOTIATIONS, AND ON-GOING FEDERAL COUNCIL MEETINGS AT BRIONI ALSO INDICATE YUGOSLAVIA IS ATTEMPTING COME UP WITH MORE EFFECTIVE POLICY IN THIS AREA. COLANOVIC'S REMARKS SUGGEST THAT A MORE COMPEHENSIVE LIBERALIZATION OF JOINT VENTURE LAW THAN PREVIOUSLY INDICATED TO US IS UNDER CONSIDERATION. HOWEVER YUGOSLAVS HAVE FOR PAST ONE AND HALF YEARS TOLD US OF INTENTION TO REVISE LAW AND COLANOVIC'S STATEMENT THAT IT WILL BE ACCOMPLISHED COMPREHENSIVELY IN 1975 MAY REFLECT MORE HIS HOPES THAN ASSURED PROSPECTS.

20. STOJILKOVIC'S SUGGESTION FOR US MISSION TO VISIT YUGOSLAV FIRMS WITH EXPERIENCE IN LDCS STRIKES EMBASSY AS POSITIVE AND LIMITED OFFICIAL USE

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PAGE 04 BELGRA 02494 02 OF 02 201542Z

TIMELY. DARINKA TRBOVIC OF OPIC WAS AT MEETING AND HAS AGREED INVESTIGATE US INTEREST IN IDEA. EMBASSY ENCOURAGES THIS AND IS READY TO HELP ORGANIZE VISIT.
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